

The Honorable Charles B. Rangel
Testimony Before House Budget Committee
Hearing on “Federal Revenue Options”
October 6, 2004

Chairman Nussle and Congressman Spratt, I am very pleased to participate in your hearing on fundamental tax restructuring.

I am rather surprised that these hearings are being held by this Committee rather than the Committee on Ways and Means. Perhaps it is a recognition by this Committee that only tax increases, disguised as fundamental tax reform, can address the long-term fiscal problems faced by our country.

The Republicans took control of the House of Representatives in 1994 with big promises to “pull the tax code out by its roots” and substitute a simpler, fairer tax system. Despite that rhetoric, the Republican Congress has enacted legislation since 1994 that has dramatically increased the complexity of our current tax system:

- According to the Internal Revenue Service, today it takes an average middle-income American family 7½ hours longer to fill out their Federal income tax return than it did in 1994, an increase from 11½ hours in 1994 to 19 hours today.
- Since 1994, the Republican-controlled House of Representatives has successfully initiated 42 new laws with 3,533 changes to our tax code contained in more than 10,000 additional pages of complex public laws.

Millions of Americans now are required to fill out two Federal income tax returns each April 15th, the regular tax return and the alternative minimum tax (AMT) return. All of this complexity is due to the decision by the Bush Administration to use the AMT to take back many of the benefits promised in the big print of the 2001 Bush tax cut. Before the Republicans took control, only 369,000 individuals were subject to the AMT.

President Bush has continued to complicate our tax law. Even conservative economist Bruce Bartlett concedes that “over the past three and a half years, Bush has made the tax code more complicated.”

Now it appears that the Republican House Leadership intends to use the complexity of our current system, much of which they are responsible for, to argue for tax reform.

Frankly, I enthusiastically support efforts to reform and simplify our current system. I am hopeful that the rhetoric will be followed by action, unlike what has happened in the past. The only issue that may divide me and some of the other members of this panel is whether we should attempt to reform our current income tax system, or enact a new tax on consumption. Although our current tax system is too complex, I strongly dispute the notion that abandoning it in favor of a more consumption-based system is the magic cure-all.

I think Representative Linder’s national retail sales tax proposal (H.R. 25) is an especially bad idea and have detailed why in a recent report issued by my Ways and Means staff, which I submit along with this testimony. To summarize:

- It is extraordinarily regressive. The effective tax rates under Rep. Linder’s bill would start at over 30% at the bottom of the income scale, and then decline to 5% at the very top. This is the reverse of the current law pattern of effective rates.
- The Linder bill would impose over \$300 billion per year in unfunded mandates on State and local governments in the form of sales taxes on their purchases.
- It repeals all current-law deductions and credits, including current-law benefits for healthcare and housing.

- It repeals the charitable deduction at a time when the Republicans are attempting to place more burdens on the charitable sector.

The other proposals for fundamental tax reform discussed at this hearing are essentially the same. They may be more complicated than Rep. Linder's bill, but they essentially are all taxes on consumption, and they all are quite regressive. Any doubt over their regressivity was eliminated when one of the architects of the Arme y flat tax (who will be on the panel of economists) described the flat tax as "a tremendous boon for the economic elite."

Rep. Linder's bill and Rep. English's bill also dramatically change the nature of our Social Security system. Both essentially repeal the current payroll taxes used to fund the Social Security system. They replace the revenue through new consumption taxes.

These taxes will place large burdens on the elderly since they apply to all goods and services, including healthcare, long-term care, and prescription drugs. Essentially, the elderly will be forced to pay twice for their Social Security and Medicare benefits, once during their working years, and again when they purchase goods and services in their retirement.

I believe that everyone should examine with care the studies conducted by the Treasury Department during the Reagan Administration. Those studies considered several different alternatives for tax reform, including consumption tax proposals very similar to the ones being proposed today.

The conclusion of the study insofar as a retail sales tax is concerned was straightforward:

"Because of its inherent regressivity, a Federal, value-added tax, or other form of general sales tax, should not be adopted as a total replacement for the income tax—the disadvantages are regressivity, a one-time increase in

prices, Federal intrusion into the sales tax area, and compliance costs of a new Federal sales tax.”

All other consumption tax proposals also were rejected by the Reagan Treasury Department, and I believe that an objective analysis of the various consumption tax proposals being discussed today would reach conclusions similar to the Reagan Administration.

Therefore, I believe that instead of talking about a radical and frankly unrealistic switch to a broad-based consumption tax, we should begin the difficult task of reforming our current income tax system.